Supreme Court, U.S.
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No. 91-571

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

ROBERT J. TAYLOR, Trustee,

Petitioner,

v.

FREELAND & KRONZ, a Partnership; WENDELL G. FREELAND; and RICHARD F. KRONZ,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

REPLY BRIEF FOR PETITIONER

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REPLY BRIEF FOR PETITIONER

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1. Respondents concede that there is a "conflict in the Circuits on th[e] issue . . . " presented by the Petition, but claim that the conflict is "minimal" because the decisions of the Fifth, Sixth, and Eighth Circuits are "factually distinguishable" from the present case. Opp. at

6. However, as the court below (the Third Circuit) acknowledged, its holding plainly and simply "disagree[d] with the conclusion reached . . . by the Courts of Appeals for the Sixth and Eighth Circuits." Appendix to the Petition for Certiorari ("App.") at 8a-9a.[1]

The court below held that if neither the trustee nor any other party in interest files an objection to a claimed exemption within the thirty-day period specified by Bankruptcy Rule 4003(b), the exemption must be allowed, regardless of whether there was any legal basis for claiming it. App. 9a, 15a. Conversely, the Fifth, Sixth, and Eighth Circuits have held that even if a timely objection is not filed, the claimed exemption should not be allowed unless there was "a good-faith statutory basis" for claiming it.

Respondents claim that the Fifth Circuit's decision in *Sherk* is "distinguishable" because the Fifth Circuit, in finding that there was no good-faith statutory basis for the exemption claimed by the debtor in that case, relied upon the fact that the debtor did not have possession of the disputed property. Opp. 10-11; 918 F.2d at 1175-1176. But the conflict between the Fifth Circuit's decision and the decision of the court below lies in the fact that the Fifth Circuit required the debtor to have a good-faith basis for the claimed exemption, not in the specific details of why such a basis did or did not exist. *See* 918 F.2d at 1174.

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[1] The court below was evidently unaware, at the time that it decided this case, of the Fifth Circuit's decision in *Sherk v. Texas Bankers Life & Loan Ins. Co. (In re Sherk)*, 918 F.2d 1170, 1174 (5th Cir. 1990).

Respondents also claim that the Eighth Circuit's decision in *Halverson v. Peterson* (*In re Peterson*), 920 F.2d 1389 (8th Cir. 1990) is distinguishable because (1) in that case, the exemption was ultimately allowed and (2) because the trustee in that case was more prompt in objecting to the exemption claimed by the debtor. Opp. at 9. However, it is irrelevant that the Eighth Circuit in *Peterson* found that there was a good-faith statutory basis for the exemption claimed in that case (920 F.2d at 1394); the point is that (unlike the court below) the Eighth Circuit would not have allowed the exemption unless the debtor had a good-faith basis for claiming it. 920 F.2d at 1393-1394. Nor is it relevant that the trustee in *Peterson* filed his objection to the claimed exemption "only" four days late; the point is that, like Taylor, the trustee in *Peterson* failed to file a formal objection within the thirty-day period.[2] Moreover, Taylor, the trustee in the present case, specifically advised respondents just *three* days after the creditor's meeting (and thus well within the thirty-day period) that he considered the net proceeds of Davis' lawsuit to be an asset of the bankruptcy estate. Petition for Certiorari 11 (citing ROA 73). Thus, although Taylor failed to file a formal objection at that time, it is disingenuous for respondents to suggest that he "has never objected to the debtor's claim of exemption." Opp. 9.

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[2] Indeed, the only reason that the trustee in *Peterson* was so "prompt" in filing his formal objection was that the debtors informed him, on the thirtieth day of the thirty-day period, that the thirty-day period had expired. 920 F.2d at 1390. Taylor did not receive any such notification in this case.

Finally, in *Munoz v. Dembs* (*In re Dembs*), 757 F.2d 777 (6th Cir. 1985), the Sixth Circuit clearly held, contrary to the decision of the court below, that exemptions will not be allowed, even when no timely objection is filed, unless there is "a good-faith statutory basis for exemption . . . " *Id.* at 780. While respondents characterize this holding as "dicta" (Opp. 9), at least two federal courts of appeals have expressly recognized *Dembs* as the law of the Sixth Circuit. *See Peterson*, 920 F.2d 1389, 1393 (8th Cir. 1990) ("This approach [requiring a good-faith statutory basis for the claimed exemption] originated in *Munoz v. Dembs* (*In re Dembs*)."); *Taylor*, App. 8a ("[t]wo federal courts of appeals have adopted [the middle-ground] approach.") (citing *Peterson* and *Dembs*).

In short, there is a clear conflict among the circuits on this important and recurrent issue. Only this Court can resolve that conflict and provide the necessary uniformity in the administration of the Bankruptcy Code.

2. Respondents also claim that this case is "moot" because the bankruptcy court "discharged" the trustee (Taylor) on June 28, 1991. Opp. 15-16. However, that claim is frivolous. It was never the intention of the bankruptcy court to discharge the trustee, and indeed that court has recently vacated the so-called order of discharge *nunc pro tunc*.

On June 26, 1991, the bankruptcy court entered an order closing the case "pending resolution of . . . " the instant action. Amended Order of Court, June 26, 1991 (attached hereto as Appendix A). That order specifically stated that "[t]he Trustee reserves the right to prosecute

the action and administer any fund generated as a result of the appeal, and distribute such fund to creditors in accordance with the provisions of the Bankruptcy Code. Such closing of the case shall in no way be deemed an abandonment of the action or of the lawsuit proceeds." *Id.* However, as a result of a clerical error, an order was issued two days later which erroneously stated that "[t]he estate of the above named debtor has been fully administered" and that the trustee was therefore "discharged." Taylor subsequently filed a motion to vacate that order, and the bankruptcy court, after admitting that it had never intended to discharge the trustee and stating that it intended to correct its own error, vacated the orders closing the case and discharging the trustee, *nunc pro tunc*, as of June 26, 1991. Order of Court, November 5, 1991 (attached hereto as Appendix B).[3]

3. The issue presented by this case--whether a debtor may obtain a groundless exemption solely because no party in interest filed a formal objection within the time allotted by Bankruptcy Rule 4003(b)--is an issue of importance in any individual Chapter 7 bankruptcy. As noted in the Petition, it has received an extraordinary amount of attention in the lower federal courts and has been fiercely debated for over seven years. Petition for Certiorari 15-18. Six federal courts of appeals have

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[3] The bankruptcy court's comments about the original order are contained in an audio tape of the hearing on the Motion to Vacate which took place on November 5, 1991. Counsel for petitioner have a copy of the tape.

divided evenly over how it should be resolved. *Id.* There is no good reason for delaying this Court's consideration of the issue.

In 1989 alone, over 420,000 individual Chapter 7 cases were filed in the federal courts. Petition for Certiorari 20. Given the current state of the economy, that number can only be expected to increase. It is therefore important that this Court now act to resolve the conflict among the circuits as to whether debtors are to be rewarded for claiming groundless and fraudulent exemptions.

CONCLUSION

The petition for certiorari should be granted.

Respectfully submitted,

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November 1991

APPENDICES

Appendix A

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF PENNSYLVANIA

In Re:	:	Bankruptcy No. 84-2291
	:	Adversary No. 88-446
EMILY DAVIS, a/k/a	:	Motion No. 91-3573M
EMILY WINN,	:	Chapter 7
	:	

AMENDED ORDER OF COURT

AND NOW at Pittsburgh in said District this 26th day of June, 1991, after notice and hearing on the above-captioned matter, it is hereby ORDERED, ADJUDGED and DECREED as follows:

1. The case is closed pending resolution of the Trustee's pending motion for judgment and to proceed to execution against assets of the debtor, and the Trustee's action as defined below.

2. In the event that the Trustee prevails in the Third Circuit Court Appeals in the Complaint to A oid Post-petition transfers Under 11 U.S.C. Sec. 549 and Sec. 550. (The Action), the Trustee will file a Motion to Reopen the above-referenced case.

The Trustee reserves the right to prosecute the action and administer any fund generated as a result of the appeal, and distribute such fund to creditors in accordance with the provisions of the Bankruptcy Code.

Such closing of the case shall in no way be deemed an abandonment of the action or of the lawsuit proceeds.

BY THE COURT:

/s/ Bernard Markovitz

Appendix B

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF
PENNSYLVANIA

In Re:	Bankruptcy No. 84-2291 BM
EMILY DAVIS, a/k/a EMILY WINN,	
Debtor,	Chapter 7
ROBERT J. TAYLOR, Trustee,	
Movant,	
vs.	Motion No. 91-7117M
FREELAND & KRONZ, a partnership; WENDELL G. FREELAND, RICHARD F. KRONZ; and EMILY DAVIS,	
Respondents.	

ORDER OF COURT

AND NOW, to-wit, this 5th day November, 1991, upon consideration of the Trustee's Motion for Relief

from Orders Closing Case and Discharging Trustee, after notice and hearing, it is hereby ORDERED that:

1. The Order entered June 26, 1991, closing the Chapter 7 proceeding of Emily Davis a/k/a Emily Winn, Bankruptcy No. 84-2291 is hereby vacated *nunc pro tunc* as of June 26, 1991;

2. The Order discharging Robert J. Taylor as Trustee is hereby vacated *nunc pro tunc* as of June 26, 1991; and

3. The Trustee is hereby authorized to proceed in execution against assets of the Debtor.

/s/ Bernard Markovitz
United States Bankruptcy Court